

Message Text

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ACTION ARA-10

INFO OCT-01 ISO-00 FEA-01 ERDA-05 AID-05 CEA-01
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USIA-06 OES-07 SP-02 SS-15 STR-04 TRSE-00 ACDA-07
PA-01 PRS-01 /102 W
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FM AMEMBASSY SANTIAGO
TO SECSTATE WASHDC 4888
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E.O. 11652: N/A
TAGS: EMIN, EINV, CI
SUBJECT: PROSPECTS FOR LARGE SCALE MINING INVESTMENTS IN CHILE:
THE CASE OF SUPERIOR OIL/FALCONBRIDGE

REF: SANTIAGO 2904

1. SUMMARY: WHILE NEGOTIATIONS OVER SUPERIOR/FALCONBRIDGE
INVESTMENT PROPOSAL CAME VERY CLOSE TO FRITION, LAST MINUTE
DIFFICULTIES DEVELOPED OVER WHETHER SUPERIOR WOULD BE PERMITTED
TO IMPORT PETROLEUM FREE OF DUTY AND TAX. PRESENT GOC POSITION
REQUIRING PAYMENT OF SUCH DUTIES AND TAXES IS CAUSING SUPERIOR
TO RECALCULATE IS PROJECTED COST. ALL OTHER OUTSTANDING ISSUES
HAVE BEEN RESOLVED, PARTICULARLY THAT OF WHETHER SUPERIOR
WILL BE ABLE TO IMPORT TAX AND DUTY FREE INVESTMENT GOODS,
WHILE GIVING GOC EFFECTIVE WAY TO INSURE ADEQUATE LEVEL OF LOCAL
PROCUREMENT. FURUTE INVESTMENTS WILL BE MADE UNDER REVISED INVEST-
MENT LAW WHICH, ON THE FACE OF IT, PRECLUDES NEGOTIATION ON
SUCH CARDINAL ISSUES AS DEPRECIATION AND RATE OF TAXATION. CHILE'S
NEGOTIATOR FOR COPPER INVESTMENT, ARTURO MACKENNA, ASSERTS THAT
GREATER FLEXIBILITY THAN PERMITTED BY THE NEW LEGISLATION IS NEEDED
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AND WILL BE FORTHCOMING. END SUMMARY.

2. SIGNIFICANCE OF THE NEGOTIATION: THIS JOINT U.S.- CANADIAN
PROJECT TO DEVELOP A LARGE OREBODY LOCATED ON THE ARGENTINE BORDER
OPPOSITE THE NORTHER PORT OF IQUIQUE, AT A COST OF APPROXIMATELY
US\$500 MILLION AND AN OUTPUT OF 100,000 MT OF COPPER PER YEAR,
WILL BE THE FIRST MAJOR FOREIGN MINING INVESTMENT APPROVED SINCE

THE SEPT. 11, 1973 CHANGE IN GOVERNMENT. THE FORMULA OF 51 PERCENT FOREIGN AND 49 PERCENT CHILEAN, TOGETHER WITH THE OTHER ISSUES BEING HAMMERED OUT IN PRESENT NEGOTIATIONS, WILL PROBABLY SET THE PATTERN FOR ALL FUTURE PROJECTS OF THIS TYPE.

3. CHILE'S CHIEF NEGOTIATOR FOR LARGE SCALE MINING PROJECTS, ARTURO MACKENNA, INFORMS US THAT THE GOC CAME VERY CLOSE TO SIGNING A CONTRACT WITH SUPERIOR OIL/FALCONBRIDGE (HEREAFTER REFERRED TO AS SUPERIOR) TO DEVELOP THE QUEBRADA BLANCA OREBODY. A SNAG, HOWEVER, DEVELOPED AT THE LAST MINUTE AND, ON MAY 13, THE SUPERIOR NEGOTIATORS WENT HOME. WHETHER SUPERIOR WILL BE PERMITTED TO IMPORT PETROLEUM FREE OF DUTY AND TAX WAS THE STUMBLING BLOCK. THE MINISTER OF MINES IS REPORTED OPPOSED TO SUCH TAX CONCESSIONS ON GROUNDS THAT ALL OTHER LARGE MINING VENTURES WOULD DEMAND THE SAME. SUCH CONCESSIONS WOULD SO REDUCE THE RELATIVE COST OF OIL AS TO UNDERMINE PRESENT GOC POLICY OF FOSTERING A SUBSTITUTION OF COAL FOR OIL.

4. SUPERIOR CONTENDS THAT ENTIRE COST PROJECTION WAS BASED ON PETROLEUM BEING FREE OF TAX AND DUTY, AND THAT AN AGREEMENT COULD NOT BE SIGNED IF GOC INSISTED ON MEASURE WHICH WOULD RESULT IN SUCH SUBSTANTIAL COST INCREASES. MINISTER OF MINES VALENZUELA THEN SUGGESTED THAT SUPERIOR COMPUTE ITS COST ON THE BASIS OF TAXED PETROLEUM, THEN CALCULATE HOW MUCH THE CHILEAN EQUITY POSITION IN THE PROJECT WOULD HAVE TO BE LOWERED, AND THAT OF SUPERIOR INCREASED, IN ORDER THAT THE INCREASED INCOME TO SUPERIOR WOULD OFFSET ITS INCREASED COST. SUPERIOR AGREED. IT REPORTEDLY BELIEVES THAT THE RECALCULATED DATA WILL BE READY 30-40 DAYS FROM NOW.

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5. SUPERIOR'S PRESIDENT KECK IS UNDERSTOOD, HOWEVER, TO BE LEERY OF A SOLUTION WHICH WOULD LOWER THE CHILEAN EQUITY POSITION IN THE PROJECT, BELIEVING THAT, ONCE COPPER PRICES BEGAN TO RISE, THE COMPANY WOULD APPEAR TO BE REALIZING WINDFALL PROFITS. UNLESS THE CHILEAN EQUITY POSITION AND INCOME WERE NEARLY EQUAL TO SUPERIOR'S, POPULAR RESENTMENT MIGHT ENDANGER SUPERIOR'S POSITION.

6. MACKENNA ALSO OPPOSES SUCH A SOLUTION FOR SAME REASON, POINTING OUT THAT ASSUMING SUCH AN EQUITY/PETROLEUM TAX TRADE-OFF, THE CHILEAN EQUITY SHARE MIGHT FALL AS LOW AS 30 PERCENT. MACKENNA IS PUSHING FOR GRANTING TAX EXEMPTION TO SUPERIOR AND, IF NECESSARY, EXTENDING SIMILAR EXEMPTIONS TO ALL LARGE SCALE MINING PROJECTS.

7. BEFORE IMPASSE ON PETROLEUM DUTY/TAXES DEVELOPED, ALL OTHER OUTSTANDING ISSUES HAD BEEN RESOLVED. PREVIOUSLY, THE BIGGEST DIFFICULTY HAD BEEN HOW TO GIVE SUPERIOR BLANKET

EXEMPTIONS FROM IMPORT DUTIES AND VALUE ADDED TAX FOR ALL
INVESTMENT GOODS WHILE AT SAME TIME REQUIRING PURCHASE OF CHILEAN
GOOD WHERE THESE WERE AVAILABLE IN SUFFICIENT QUANTITY AND
QUALITY.

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ACTION ARA-10

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8. SOLUTION WAS TO REQUIRE APPROVAL OF THE BOARD OF THE NEW
MIXED COMPANY FOR ALL IMPORTS. CHILEAN DIRECTORS ON THE BOARD
WOULD BE OUTNUMBERED 4 TO 3; SUPERIOR COULD THUS ALWAYS OVERRIDE
CHILEAN OPPOSITION TO IMPORTED EQUIPMENT. HOWEVER, IF CHILEAN
BOARD MEMBERS WERE TO DISAGREE AND WERE TO BE SUPPORTED BY THE
PRESIDENT OF THE CENTRAL BANK AND FINANCE MINISTER, SUPERIOR
WOULD BE REQUIRED TO PAY IMPORT DUTIES AND VALUE ADDED TAX
ON ITEMS UNDER CONTENTION. IN SUCH A CASE SUPERIOR WOULD HAVE
FURTHER RECOURSE TO THE CUSTOMS COURTS. THE IMPORTANT POINT,
HOWEVER, IS THAT SUPERIOR WOULD BE ENABLE TO GO AHEAD AND MAKE
THE IMPORTS IT DEEMED TO BE NECESSARY WITHOUT AWAITING PRIOR GOC
APPROVAL, LEAVING DIFFERENCES OVER TAXES AND DUTIES TO BE SETTLED
LATER.

9. MACKENNA RELATED THAT SUPERIOR PRESIDENT KECK MADE SPECIAL POINT
OF EMPHASIZING THAT HIS INVESTMENT WAS BEING MADE UNDER THE OLD
VERSION OF THE INVESTMENT CODE (DECREE LAW 600). THIS REPORTEDLY
RAISED HACKLES OF FINANCE MINISTER SERGIO DE CASTRO, WHO FEELS
CONSIDERABLE PRIDE OF AUTHORSHIP CONCERNING THE NEW INVESTMENT
CODE. BASIC DIFFERENCE BETWEEN NEW AND OLD VERSION LIES IN DEGREE
OF FLEXIBILITY. UNDER THE ORIGINAL LEGISLATION, ISSUES SUCH
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AS TAXES AND DEPRECIATION WERE MADE SUBJECT TO NEGOTIATION BETWEEN THE INVESTOR AND THE FOREIGN INVESTMENT COMMITTEE. THE REVISED CODE SIMPLY MAKES THE FOREIGN INVESTMENT SUBJECT TO CHILEAN LAW IN ALMOST ALL CASES.

10. MACKENNA CLAIMS THAT HE OPPOSED DE CASTRO'S CONCEPT FROM THE VERY BEGINNING. IN ARGUMENTS OVER WISDOM OF THE INVESTMENT CODE REVISION, HE ALWAYS POINTED OUT THAT CHILEAN LAW HAS DONE A VERY POOR JOB OF ENCOURAGING DOMESTIC, NOT TO MENTION FOREIGN, INVESTMENT. IN FACT, HE ASSERTS THAT MOST OF THE INVESTMENT ACTIVITY INVOLVES PURCHASE OF EXISTING FIRMS RATHER THAN THE CREATION OF NEW ONES.

11. EMBOFF QUESTIONED WHETHER, IN VIEW OF PROVISIONS OF NEW INVESTMENT LAW, THERE WILL IN FACT BE SUFFICIENT ROOM FOR NEGOTIATION. MACKENNA NOTED THAT ALL MATTERS AS IMPORTANT AS THESE WILL IN FACT BE SUFFICIENT ROOM FOR NEGOTIATION. MACKENNA NOTED THAT ALL MATTERS AS IMPORTANT AS THESE WILL INEVITABLY BE SUBJECT TO NEGOTIATION, WHATEVER THE NEW LAW MAY SAY. HE SAYS THAT HE POINTED THIS OUT TO PINOCHET HIMSELF. IN SHORT, MORE FLEXIBILITY, EITHER BY LEGISLATIVE AMENDMENT OR INTERPRETATION, WILL HAVE TO ACCOMPANY THE IMPLEMENTATION OF CHILE'S NEW INVESTMENT LAW, AND THIS WILL BE ESPECIALLY TRUE FOR LARGE SCALE PROJECTS IN THE MINING SECTOR. POPPER

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